

**INTERNAL REVENUE SERVICE
ADVISORY COUNCIL**

**WAGE AND INVESTMENT
SUBGROUP REPORT**

**ANN ESARCO, SUBGROUP CHAIR
TARA ANTHONY
DONNA BAKER
ERNEST HICKS
WILLIAM PHILBRICK
ANDRE' RE**

NOVERMBER 15, 2012

INTRODUCTION/EXECUTIVE SUMMARY

The IRSAC Wage & Investment Subgroup (hereafter “Subgroup”) is comprised of a diverse group of tax professionals including Certified Public Accountants, Enrolled Agents, educators, and (Volunteer Income Tax Assistance) VITA site managers. The members of this group have a wide range of experience in taxation, including both preparation of tax returns and representation of taxpayers. We are honored to serve on the IRS Advisory Council and appreciate the opportunity to submit this report.

The Subgroup would like to thank W&I Commissioner Peggy Bogadi for her recognition of the value of the Subgroup as an integral part of her leadership team. The Subgroup has had the privilege of working with the professionals within the W&I operating division of the IRS and found them to be extremely helpful in providing the information, resources, guidance, and IRS personnel necessary to develop our report. We also appreciate the support provided by our designated liaisons who do a masterful job at navigating the IRS and ensuring that we have access to the necessary information to develop our analysis and issue our report.

The Subgroup has researched and is reporting on the following four issues:

1. Reporting of Dispositions of Capital Assets on Forms 1099-B (Proceeds from Broker and Barter Exchange Transactions), 8949 (Sales and Other Disposition of Capital Assets), and Schedule D (Capital Gains and Losses) (Form 1040)

The W&I Subgroup of IRSAC was asked to assist the IRS by reviewing the 2012 Form 8949 “Sales and Dispositions of Capital Assets” and Form 1099-B “Proceeds From Broker and Barter Transactions,” including their respective instructions. These forms provide data that flow into Schedule D “Capital Gains and Losses” (Form 1040).

The forms and processes are well thought out and can be expected to increase the efficiency of the information-matching program. We offer suggestions, such as formatting changes, clearer use of terminology, and consistent reporting requirements for dollars that are pertinent in capturing the proper gain or loss on each transaction. We also suggest that the IRS change some of the 2011 format standards, for example, landscape mode, single spacing, and the required reporting of number of shares sold per transaction.

2. Increase BMF Electronic Filing

The IRS requested that the W&I Subgroup of IRSAC provide recommendations to increase electronic filing of business tax returns. In addition to recommending ways of increasing e-filing of business tax returns, the subgroup was also asked for assistance in communicating with the practitioner and business communities the advantages of e-filing business tax returns.

3. Practitioner Priority Service (PPS) — Redirecting Practitioners to IRS Automated Applications

The W&I Subgroup of IRSAC was asked to provide assistance with recommendations for exploring options to encourage more practitioners to utilize automated services. The IRS would like to increase practitioner reliance on e-service tools and decrease reliance on one-on-one contact through the IRS Practitioner Priority Service (PPS). Transferring practitioners to e-services when appropriate can increase assistor availability for issues that require an assistor's support.

4. EITC Central — Electronic Toolkit

The W&I Subgroup of IRSAC was asked to provide recommendations on how to best market EITC (Earned Income Tax Credit) Central to the practitioner community and

specifically increase the use of the Spanish version of the Due Diligence Training Module. We find that EITC Central and the Return Preparer Toolkit are excellent resources for the practitioner. We offer suggestions on making these resources more easily accessible and available in both English and Spanish.

The report also suggests changes to the continuing education requirements for practitioners and offices that prepare more than ten EITC returns annually, outreach strategies to those that self-prepare returns with EITC, and exploring other avenues of validating EITC claims.

**ISSUE ONE: REPORTING OF DISPOSITIONS OF CAPITAL ASSETS ON
FORMS 1099-B (PROCEEDS FROM BROKER AND BARTER EXCHANGE
TRANSACTIONS), 8949 (SALES AND OTHER DISPOSITION OF CAPITAL
ASSETS), AND SCHEDULE D (CAPITAL GAINS AND LOSSES) (FORM 1040)**

Executive Summary

The Subgroup was asked to assist the IRS by reviewing the 2012 Form 8949 “Sales and Dispositions of Capital Assets” and Form 1099-B “Proceeds From Broker and Barter Transactions”, including their respective instructions. These forms provide data that flow into Schedule D “Capital Gains and Losses” (Form 1040).

The forms and processes are well thought out and can be expected to increase the efficiency of the information-matching program. We offer suggestions, such as formatting changes, clearer use of terminology, consistent reporting requirements for dollars that are pertinent in capturing the proper gain or loss on each transaction. We also suggest that the IRS change some of the 2011 format standards, for example, landscape mode, single spacing, and the required reporting of number of shares sold per transaction.

Background

Form 1099-B and Schedule D were substantially revised for the 2011 tax year. Form 8949 was also developed and released for 2011. The purpose of these revisions and form development was to provide the IRS with more accurate computer matching outcomes for transactions reported on Schedule D.

Based on feedback from taxpayers, practitioner focus groups, and organized public forums like IRPAC, the IRS plans to require additional information on Form 8949 along with substantial revisions to the layout of the form beginning with tax year 2012.

The W&I operating division of the IRS has requested feedback from the Subgroup on the proposed changes.

Recommendations

Form 8949

1. Format Form 8949 in landscape mode to accommodate easier reporting of additional information.
2. Format at single-space to allow for more transactions per form. Double-spacing would not be necessary with columns for stock symbol and number of shares in addition to description of property column. Adequate information to identify the transaction would be readily available with the multi-column description format.
3. Provide for reporting of both short-term and long-term on one page, which can be accomplished with the form design remaining at single-space.
4. Add column for gain or loss calculation per transaction. This provides valuable output data for the taxpayer.
5. Add separate columns for stock symbol and number of shares per transaction. This provides for more consistent data input and provides an audit trail for both the taxpayer and tax return preparer.
6. Move exception code cell next to adjustment cell that the code is defining instead of at the beginning of transaction line. This assists the taxpayer with understanding the purpose and meaning of the code.
7. Change last sentence of Part 1 and Part 2 NOTE by deleting “or more of the boxes” since at this time, only one box can be checked per Form 8949. (Reference Form 8949, 2012 draft as of May 22, 2012)

8. Change last sentence of asterisk note under boxes A, B, and C to read, “Basis is required to be reported by *brokerage firms* to the IRS for most stock you bought in 2011 or later.” (Reference Form 8949, 2012 draft as of May 22, 2012)
9. Change Part II, line 1, to Part III, line 3. (Reference Form 8949, 2012 draft as of May 22, 2012)
10. Edit wash sale instructions, last paragraph (d-4) to state “with the appropriate box A, B, or C, checked” rather than “with the appropriate box checked.”
11. Require filing of Form 8949 with tax returns only when 1099-B forms do not include basis for all transactions reported.

Form 1099-B

1. Remove option for box 2a to report either gross proceeds or gross proceeds less commissions and options premiums. Require that all sales are reported net of commissions and premiums.
2. Change labeling of “covered and non-covered securities” to “covered and non-covered transaction dates.” The term “covered securities” has a particular definition within the financial securities industry. The IRS use of the term “covered securities” creates confusion because the IRS definition does not agree with the industry standard.
3. Require brokerage firms to report quantity of shares sold for each transaction.
4. Edit the instructions to 1099-B, boxes 13-15 to state, “shows state income tax information” rather than “shows state income tax withheld.”

5. Refer to IRPAC the development of guidelines to brokerage firms to consistently handle reporting of employee stock options, brokerage stock options (covered and non-covered), and wash sales.

ISSUE TWO: INCREASE BMF ELECTRONIC FILING

Executive Summary

The IRS requested that the Subgroup provide recommendations to increase electronic filing of business tax returns. In addition to recommending ways of increasing e-filing of business tax returns, the Subgroup was also asked for assistance in communicating with the practitioner and business communities the advantages of e-filing business tax returns.

Background

While there continues to be an increased percentage in individual e-filed returns, the percentage of electronically filed employment tax returns is somewhat stagnant; see Table 1: Statistic of E-filed Tax Returns from 2009 through 2011. Most businesses file five employment tax returns per year (four quarterly Forms 941 and one annual Form 940). The Subgroup believes that by increasing e-filing employment tax returns, there will be an increase in e-filing of other business tax returns. Focusing on employment tax returns has the potential to affect a larger portion of the business population than focusing on other business tax returns. Some businesses (e.g., sole proprietorships) file employment tax returns, but not business income tax returns that are separate from Form 1040.

Table 1: Statistics of E-Filed Tax Returns from 2009 through 2011

Return Type	Processing Year	Total Returns Filed	% e-filed
Individual – Form 1040 Series	2009	143 million	67%
	2010	141 million	70%
	2011	143 million	78%
Employment – Forms 941	2009	23.3 million	23.2%
	2010	23.2 million	24.5%
	2011	23.0 million	26.8%
Employment – Forms 940	2009	5.9 million	21.6%
	2010	5.7 million	23.1%
	2011	5.6 million	24.9%

The Subgroup encourages the IRS to provide a better, more streamlined system for e-filing employment tax returns. With a streamlined system in place, the IRS can promote the value of e-filing these returns.

Recommendations

1. Encourage software vendors to include e-filing in their employment tax preparation software and link to Electronic Federal Tax Payment System (EFTPS) to electronically file returns, as an alternative to printing and mailing.

2. Link the e-filing of the Forms 941 and 940 to EFTPS to simplify the process of e-filing employment tax returns. At present, many small companies prepare the forms online or manually; and then mail rather than file online. Since employers are required to pay using EFTPS, incorporating the employment tax returns into the payment processing system would allow both (payment and filing) to be accomplished through one web portal.
3. Pursue a mandate for e-filing of employment tax returns through Modernized e-file (MeF), retaining the current minimum paper filing exception and payment amount of \$2,500 per quarter. Consideration should be given to coordinate with states that already mandate e-filing of business tax returns, especially employment tax returns.
4. Provide a secure and safe method at time of set-up for signature verification of employment tax returns.
5. Develop a simple free-file way to e-file. Because many businesses that paper file may not use software or practitioners to prepare the forms, this would not be financially harmful to software vendors or practitioners.
6. Coordinate with MeF, as necessary, to limit or eliminate the name control function to allow efficient processing of new e-filed returns without unnecessary rejections.
7. Promote the advantages of e-filing business tax returns. Use email, media, social media, IRS.gov and letters to businesses and practitioners to publicize the time and effort saved by e-filing business tax returns. Practitioners and individuals know the benefits of e-filing individual tax returns. Thus, the IRS should emphasize that the

same benefits of simplification and time and money savings will apply with e-filing of all business tax returns.

ISSUE THREE: PRACTITIONER PRIORITY SERVICE (PPS) —
REDIRECTING PRACTITIONERS TO IRS AUTOMATED APPLICATIONS

Executive Summary

The Subgroup was asked to provide recommendations for exploring options to encourage more practitioners to utilize automated services. The IRS would like to increase practitioner reliance on e-service tools and decrease reliance on one-on-one contact through the IRS Practitioner Priority Service (PPS). Transferring practitioners to e-services when appropriate can increase assistor availability for issues that require an assistor's support.

Background

Each year, Accounts Management answers 1.3 million calls annually on the PPS telephone line. The Level of Service (LOS) provided in FY2011 was 78 percent. In FY2012 due to budgetary constraints on IRS resources, the goal for LOS on the PPS line is 66 percent. Accounts Management is aware that this will cause longer practitioner wait times, increased practitioner abandons, reduced practitioner satisfaction, and an increased number of practitioners redialing the IRS toll-free lines for service.

Recommendations

1. Establish a priority Centralized Authorization File (CAF) fax number for submitting Form 2848 "Power of Attorney and Declaration of Representation" that will be used on the e-services system so that in one to two days the 2848 would be posted and available for e-services. Currently this process takes approximately ten days. It is recognized that Forms 2848 submitted through e-services is instantly available for use; however, all of the required information is

not always available to the practitioner to submit through e-services. In these instances, the practitioner may not be able to utilize the e-services method for submitting the Form 2848, for example, when the taxpayer is new to the practitioner and prior year tax returns are not available.

2. Create a scan-able Form 2848. This would allow an alternative to faxing the Form 2848 and permit electronic entry of Form 2848 into the CAF.
3. Update the message on the initial PPS greeting explaining the alternatives for obtaining information from e-services and other sources. Add to the message a reminder that recently filed returns and amended returns are not available for an extended period of time (that time period to be noted and updated as necessary).
4. Issue advisories and informational reports on systemic and/or procedural issues and their solutions or temporary fixes similar to e-file alerts.
5. Provide a notation for the first assistor to record that a valid Form 2848 was faxed and that it will be recorded in the CAF. This will eliminate the need for re-faxing the Form 2848 when a practitioner is transferred to a different assistor working the same case.
6. Provide the option for a practitioner to leave a message requesting a return call rather than being placed on hold for extended periods of time. Both the Department of Veterans Affairs and the Social Security Administration currently employ this callback method.
7. Upgrade the training of the assistors on the PPS line so that they can address issues and help solve problems on the first call. Oftentimes the practitioner has to make several calls to find an assistor that understands the problem and can

- provide a solution. Also, many of the assistors say they do not have the power to solve a problem, and they will not cooperate in finding a solution. When the practitioner places a second call to PPS and is connected to a different assistor, the practitioner may find someone who is more receptive to finding a solution.
8. Allow additional authorized persons, such as persons with a valid Form 8821 “Tax Information Authorization,” access to the TDS (transcript delivery system).
 9. Establish a methodology/procedure for practitioners to revoke a power of attorney through e-services.
 10. Create a shortcut, one-click way for practitioners to get to e-services on IRS.gov.
 11. Expand the promotion of e-services capabilities, through multi-media and print methods. A slick one-to-two page color flyer should be sent to all practitioners informing them of all the capabilities of e-services and its ease and efficiency of use.
 12. Enhance all forms of practitioner education about e-services by using all available communication methods including the IRS Nationwide Tax Forums, emails, e-alerts, and printed copy to expound on the benefits of e-services.
 13. Create a YouTube video explaining how to register with and use e-services.
 14. Set up e-service accounts for practitioners at the IRS Nationwide Tax Forums.
Showcase e-services at the forums.

ISSUE FOUR: EITC CENTRAL — ELECTRONIC TOOLKIT

Executive Summary

The Subgroup was asked to provide recommendations on how to best market EITC (Earned Income Tax Credit) Central to the practitioner community and specifically increase the use of the Spanish version of the Due Diligence Training Module. We find that EITC Central and the Return Preparer Toolkit are excellent resources for the practitioner. We offer suggestions on making these resources more easily accessible and available in both English and Spanish.

The report also suggests changes to the continuing education requirements for practitioners and offices that prepare more than ten EITC returns annually, outreach strategies to those who self-prepare returns with EITC, and exploring other avenues of validating EITC claims.

Background

Census data indicate that the EITC lifted 6.6 million individuals out of poverty in 2009, including more than three million children. The EITC lifts more children out of poverty than any other program (*Earned Income Tax Credit – Overpayment and Error Issues*, Center on Budget and Policy Priorities, April 19, 2011). To claim the credit, the taxpayer must determine eligibility by deciding if they have a qualifying child, their filing status and their income. This results in two types of errors: (1) failure to claim the credit when eligible; and (2) erroneously claiming or over-claiming the credit based on eligibility level. It is estimated that 20 percent of those eligible do not claim or receive the credit, leaving as much as \$1 billion unclaimed. The estimate of improper payments for fiscal year 2011 is approximately 21 percent to 26 percent, or nearly \$15.2 billion

(The Department of the Treasury Annual Financial Report, Fiscal Year 2011, November 2011).

The most common errors that result in improper payments are: (1) claiming a child who does not meet the age, residency or relationship tests or claiming a child who is a qualifying child of someone with a higher AGI (36 percent); (2) claiming single or head of household when not eligible for that filing status (18 percent); and (3) under-reporting or over-reporting income (ten percent) (*Compliance Estimates for Earned Income Tax Credit Claimed on 1999 Returns*, February 2002).

Paid preparers complete 62 percent of EITC returns, while 36 percent of the returns are self-prepared, and three percent are prepared by volunteers or the IRS (due to rounding, total is greater than 100 percent) (*EITC After Math Error*, EITC Office, Tax Year 2010). The IRS considers tax professionals essential partners in helping individuals and families understand the complex EITC laws. The IRS has developed numerous online tools to educate preparers and taxpayers about EITC and EITC due diligence. These online solutions are located at EITC Central, www.eitc.irs.gov.

Recommendations

1. Add an EITC icon to the IRS.gov homepage to assist in providing easy access to the Return Preparer Toolkit.
2. Add a prominent EITC icon or a direct link from the “For Tax Pros” page to the Toolkit. Currently, access is provided under “other tools and information.” From there, one clicks “basic tools for Tax Pros” and then “EITC Electronic Toolkit for Tax Preparers,” which requires the user to leave the IRS website to finally access the Tax Preparer Toolkit.

3. Leverage social media to market EITC Central and the Return Preparer Toolkit.

Using a multi-channel strategy, promotional material should be transmitted via Facebook, Twitter, LinkedIn, etc. Facebook entries could have short video clips like the “must do” video series. Twitter can have reminders on the “must do” concepts. LinkedIn could have a discussion on the EITC.

4. Edit PowerPoint presentation located at

www.eitc.irs.gov/rptoolkit/toolsandtips/commonduediligencesituations.

- a. Revise numbering of examples in the five PowerPoint presentations under Handling Common Situations. These are excellent, but apparently were part of one larger PowerPoint presentation. The examples within each presentation are numbered continually from presentation to presentation. Each presentation’s examples should start with its own numbering.
- b. Provide an example of what a diligent reconstruction of income may entail on presentation titled “Self-Employed House Cleaner.”
- c. Add scenarios for “Social Security Card” presentation to provide scenario for the Permanent Resident Card and the Social Security Card Not Valid for Employment.
- d. Acknowledge the illegal practice of selling of dependents for tax benefits in presentation titled “Additional Qualifying Child.”
- e. Update the tax years in Scenarios 1 and 2 under “Qualifying Child Scenarios.”

5. Provide access to all due diligence video clips located at

www.eitc.irs.gov/rptoolkit/ddvideos on YouTube. Currently the video clips must

be downloaded, and then played. Access on YouTube would permit sharing of the videos on social media platforms and playing on tablets and smart phones.

6. Increase prominence of the Due Diligence video clips. These clips are both educational and entertaining. Place an EITC icon on the For Tax Pros landing page, as well as on the IRS.gov homepage, announcing free continuing education credits. Make it one click from the For Tax Pros landing page to the video clips.
7. Create modules using the Due Diligence video clips and the PowerPoint presentations. For example, the “Self-Employed House Cleaner” PowerPoint could be grouped with the “Recordkeeping,” “Audit” and “Schedule C Recordkeeping” video clips. These two educational delivery methods presented in one place for quick review provide for better understanding of these complex matters.
8. Translate all of the video clips and PowerPoint presentations into Spanish. The video clips could be dubbed over to reduce cost of re-production.
9. Create a Spanish section on EITC Central. Provide a folder icon at the top, along with the EITC Central, Tax Preparer Toolkit, Partner Toolkit, and Marketing Express folder tabs. Duplicate the learning modules that are available in English on this section. Currently, English and Spanish are interspersed throughout.
10. Create a multicultural team that would develop a strategic plan for outreach to the Spanish community. According to statistics, Latinos utilize social sites 26.8 percent more frequently as compared to other minorities (Hispanics More Active On Social Media Than Other Minorities (2012), retrieved September 16, 2012, from <http://www.emarketer.com/Article.aspx?R=1008877>). Tax professional organizations may be able to provide initial outreach strategies.

11. Create “share” link on all press and news releases allowing for ease of sharing information through social media sites (e.g., Facebook and LinkedIn).
12. Generate all educational materials in Spanish and distribute through social media and other channels targeted specifically to the Spanish population. Incorporate “share” link.
13. Provide free CPE, in Spanish, on IRS.gov, targeting the Latino practitioner community.
14. Require all practitioners (including those who do not sign the return) that prepare more than ten EITC returns to complete one hour of EITC continuing education credit per year. This can be a self-declared attestation similar to the annual two hours of ethics required of Enrolled Agents and Registered Tax Return Preparers. Place the notice of this requirement on both the homepage of IRS.gov and the landing page of For Tax Pros.
15. Require all firms that prepare ten or more EITC tax returns to maintain documentation of compliance with the one hour of EITC continuing education training requirement for those who prepare more than ten EITC returns.
16. Promote the free one-hour continuing education credit provided for completing the EITC due diligence training module. Use the “Welcome to the Tax Preparer Toolkit” graphic as an entrance to EITC training modules. Currently the graphic is a group of individuals gazing at a computer. Change the graphic to a door or entranceway to “FREE EITC CPE!” or “EITC Café.” Run banner similar to IRS.gov homepage that suggest videos and PowerPoint presentations are available.

Make certain that it is only two clicks from IRS.gov to “For Tax Pros” to EITC portal.

17. Reach out to tax professional organizations and ask them to provide a link from their association website to EITC Central and the Due Diligence Training aids.
18. Distribute to all self-preparers who have claimed EITC with a Schedule C, a pre-filing season, one-page summary of IRS documentation requirements for income and expense items. Include a web link to examples that would further clarify these requirements. Incorporate this information in a prominent (first page) location in the filing instructions.
19. Distribute to all self-preparers who have claimed EITC with a Schedule C, a pre-filing season, one-page summary of audit issues related to Schedule C and EITC audits.
20. Clarify last bullet point in “What techniques can be used to obtain information from your client?” section of the “Schedule C and Record Reconstruction Training Module” dated June 13, 2012. The last three sentences read:

Taxpayer claims of having supporting documentation is not sufficient to meet tax preparer due diligence. (If a taxpayer comes in with an income statement that appears, to a reasonable person to be correct and complete, documentation would not be requested). Preparers should inquire how income and expenses were compute and document the responses. In circumstances where you feel

the information is not accurate or the supporting material is sufficient, you may ask to see the supporting material.

Perhaps the first and last sentences should be reversed. The current last sentence should state, “supporting material is insufficient.”

21. Provide a disclaimer in The Schedule C and Record Reconstruction Training module that states the techniques and practices contained therein are not standards but suggested methods and best practices, and under all circumstances, the practitioner is subject to the provisions of IRC Sec. 6695(g), the regulations thereunder and the provisions of Circular 230. This is required to avoid any confusion that the materials impart different standards to Schedule C which are mandatory and necessary to meet due diligence.
22. Revise Form 8867 “Paid Preparer’s Earned Income Credit Checklist” to be applicable to all returns and require the submission of the form for all EITC returns including returns that are self-prepared or prepared by volunteers.
23. Continue collaborating with Taxpayer Advocate Service on the pilot program testing the use of standardized third party affidavits to substantiate a child’s residency for EITC.
24. Test other methods to pre-certify that qualifying children are claimed on the allowable tax return.

**INTERNAL REVENUE SERVICE
ADVISORY COUNCIL**

**SMALL BUSINESS/SELF EMPLOYED
SUBGROUP REPORT**

**MADELEINE TOWNES, SUBGROUP CHAIR
SANFORD D. KELSEY, III
FRED F. MURRAY
CYNDI P. TROSTIN
DEBORAH WALKER
CECILY V. M. WELCH**

NOVEMBER 15, 2012

INTRODUCTION/EXECUTIVE SUMMARY

The IRSAC Small Business/ Self-Employed Subgroup (hereafter “Subgroup”) consists of six tax professionals from a wide-range of backgrounds. Its members comprise of certified public accountants, attorneys, and attorneys that act as both, all of whom serve the tax system in public and private industries, and education. The Subgroup’s membership represents a vast range of taxpayers served by the Small Business/ Self-Employed Operating Division of the Internal Revenue Service (hereafter “SB/SE”).

The Subgroup enjoys a close working relationship with the professionals within SB/SE. This relationship has granted the Subgroup the opportunity to consult with SB/SE leadership on many issues over the past year. The Subgroup focused on reducing taxpayer burden, bringing non-filers into the tax system and improving technology to improve operational efficiency. The Subgroup and SB/SE consulted both formally and informally on all issues contained in this report. The Subgroup respectfully recommends the following based upon the overarching working goals of the Subgroup. We recommend the following seven issues:

I. Reduce Taxpayer Burden

1. How Lien Withdrawal Processing Should Be Made More Efficient to the Benefit of the IRS and Taxpayers

Concerns have been raised by practitioners over the lack of a consistent approach taken on lien withdrawals between IRS offices on routine lien withdrawal matters. Streamlining decisions on such requests can provide a more consistent approach for

taxpayers while freeing up IRS personnel resources to work on more complex lien withdrawal requests.

2. **Electronic Completion and Filing Should Be Available for Form 1099-Misc**

Currently, the Form 1099-MISC cannot be filed on-line from the IRS website. Businesses that do not have a large number of these forms to complete have limited options. The ability to complete and file the Form 1099-MISC on-line would simplify a business taxpayer's compliance with this tax requirement.

3. **Encourage Taxpayers to Correct Form 1099 and Form W-2 Underreporting**

Often times a taxpayer is unsure as to what form to file. Additionally, given the volume of forms filed, some of these forms have incorrect information. In a voluntary compliance tax system, taxpayers should be encouraged not only to report and pay the proper amount of tax on originally filed information returns, but also have the ability to efficiently correct errors discovered after returns have been filed.

4. **The IRS Should Provide for a Central and Accessible Information Source so Taxpayers can Understand Required Information Reporting Rules**

Despite new statements contained in annual income tax forms (e.g., Form 1040 Schedules C, C-EZ, E, and F, and Forms 1120, 1120S and 1065) that require taxpayers to affirm their compliance with Form 1099 information reporting, there is no entry point or checklist on the IRS website or in any of the publications that allows a taxpayer to easily determine its reporting requirements. While there is information available, much of it is form specific and thus researching the specific form to file is difficult as it is really a process of trial and error.

II. IRS Non-Filer Compliance, Sustainance and, Enforcement

5. Efficiencies in IRS Outreach Can Be Created to Bring More Taxpayers into Filing and Paymanet Compliance

The IRS should consider expanding its educational outreach program to non-filer and delinquent taxpayers by focusing on small businesses and ethnic communities through a combination of public and social media, print and internet announcements, and personal contacts that will encourage filing of delinquent returns and payment of tax through (education involving) a better awareness and understanding of available installment plans, offers in compromise, penalty abatement programs, and by tax preparation assistance.

III. Opportunities for Technology Improvements

6. Use of Accounting Software During Examinations Reduces Burdens to Taxpayers and the Service, But Should Be Carefully Limited in its Implementation

Use of electronic data is an efficient examination tool for the IRS as it reduces the amount of paper generated and in some cases the time required to complete them. However, IRS requests for electronic client backup files from commercially available business software programs (e.g., QuickBooks and Peachtree) have heightened concerns by affected taxpayers and their advisers about the breadth of information requested by the IRS and the use of that information.

7. Html Pages on [irs.gov](https://www.irs.gov) Should Be Able to be Converted into PDF Format for Retention, Storage and Transfers to Clients

Generally, the information on IRS.gov is only available in HTML format which makes it difficult to share the information with others and to archive or save the

information in a file. As the website becomes the primary source and in some cases the only repository of information, the inability to easily retain and transfer the information becomes problematic.

I. Reduce Taxpayer Burden

ISSUE ONE: HOW LIEN WITHDRAWAL PROCESSING SHOULD BE MADE MORE EFFICIENT TO THE BENEFIT OF THE IRS AND TAXPAYERS

Executive Summary.

Taxpayers are hindered by having tax liens on their credit record even after the liens have been satisfied, after the taxpayer has entered into a direct debit payment arrangement, or after a determination has been made that withdrawing the lien would benefit both the IRS and the taxpayer. This is especially problematic for small business taxpayers. IRS lien procedures have been evolving quickly over the past few years, but they can be further improved by implementing better efficiencies for both the IRS and the taxpaying public.

Background

In 2011, the IRS issued over 1 million Notices of Federal Tax Lien (“NFTL”).³ In 2012, this number dropped by 41 percent.⁴ Once the NFTL is filed, the taxpayer must deal with credit issues that impact him personally and, if a small business is involved, harm the taxpayer’s ability to continue effectively transacting business.

In its 2009 and 2010 Public Reports, IRSAC suggested how to make the IRS lien procedures more effective. Since then the IRS has created efficiencies to the tax process by lessening the use of automatic liens and giving more discretion to its employees to decide when a NFTL is or is not appropriate, and when it should be released or

³ Taxpayer Advocate Service 2011 Annual Report to Congress, Vol. 2., page 93.

⁴ Taxpayer Advocate Service – Fiscal Year 2013 Objectives, citing IRS Collection Activity Report NO-5000-25 Lien Report (Apr. 2012).

withdrawn. In addition, more liberal decision making with regard to NFTL releases and withdrawals has allowed the rigors of tax collection in a harsh economy to facilitate the collection of tax dollars while aiding the taxpayers it serves. We applaud the IRS for the strides it has made since these last reports, but more remains to be done.

The focus of the 2010 IRSAC Report was on training and education. Such training should include when discretion should be used to impose a NFTL, when the NFTL should be properly released, and when the NFTL should be withdrawn.⁵ In February 2011, the IRS' *Fresh Start* program made it easier for taxpayers to obtain NFTL withdrawals.⁶ In the first year of the program, *Fresh Start* accounted for 40 percent of the withdrawal certificates issued; in the first part of 2012, the number has increased to 61 percent of total withdrawal certificates.⁷

Currently, the first step in the process of requesting the withdrawal of an NFTL is for a taxpayer or his representative to submit a letter requesting a withdrawal, or to fill out and submit Form 12277 "Application for Withdrawal of Filed Form 668(Y), Notice of Federal Tax Lien" to the IRS office assigned to the taxpayer's account. The IRS office then submits Form 13794-W, "Request for Withdrawal or Partial Withdrawal of Notice of Federal Tax Lien" to the Advisory Group office. If there is no IRS office assigned, the taxpayer's request should be mailed directly to an advisory group manager at the

⁵ IRSAC 2010 Report, Page 9-10 (Issue No. 5, Recommendations #1, #3)

⁶ Treasury Inspector General for Tax Administration, "Procedures for Withdrawals and Releases of Notices of Federal Tax Lien Were Not Always Followed," Aug. 22, 2012. No. 2012-30-096, page 4.

⁷ *Id.* at page 6.

addresses listed in Publication 4235 “Advisory Group Addresses.” Only an advisory group manager or insolvency group manager can authorize withdrawal of a NFTL.

Per IRC Section 6331, Form 12277 allows for consideration of a lien withdrawal in the following circumstances:

1. The Notice of Federal Tax Lien was filed prematurely or not in accordance with IRS procedures.
2. The taxpayer entered into an installment agreement to satisfy the liability for which the lien was imposed and the agreement did not provide for a Notice of Federal Tax Lien to be filed.
3. The taxpayer is under a Direct Debit Installment Agreement (DDIA).
4. Withdrawal will facilitate collection of tax.
5. The taxpayer or the Taxpayer Advocate acting on behalf of the taxpayer, believes that the withdrawal is in the best interest of the taxpayer and the government.

If the taxpayer is requesting a withdrawal because a lien was already released⁸, the taxpayer must meet the following requirements:

1. Tax liability has been satisfied;
2. Taxpayer is in compliance for the past three years filing all returns;
3. Taxpayer is current on all estimated tax payments and federal tax deposits, as applicable.⁹

⁸ This request would fall under #5 of the Form 12277 list of considerations for withdrawal.

⁹ Article: Fresh Start Notice of Federal Tax Liens –
<http://www.irs.gov/businesses/small/article/0,,id=23905,00.html>

If the taxpayer is requesting a withdrawal because he has entered into a DDIA, he must meet the following requirements:

1. Current amount owed must be less than \$25,000;
2. The DDIA must be payable within 60 months or before the collection statute expires, whichever is earlier;
3. Full compliance with all other filing and payment requirements;
4. Must have made three consecutive DDIA payments;
5. Cannot have previously had a lien withdrawn for the same taxes unless it was due to an improper filing;
6. Cannot have defaulted on any DDIA.¹⁰

If, upon receipt of Form 12277 or a letter requesting an NFTL withdrawal, it can be ascertained that all three criteria for withdrawal have been met with regard to an NFTL that has already been released, or that all six criteria have been met with regard to such withdrawal request due to a DDIA, there should be an approval of the request. Only if the requisite criteria are not met should it continue on for a manager's review.

Concerns have been raised by practitioners over the lack of a consistent approach taken on lien withdrawals between IRS offices on routine lien withdrawal matters, such as described above. Streamlining decisions on such requests can provide a more consistent approach for taxpayers while freeing up IRS personnel resources to work on more complex lien withdrawal requests.

Recommendations

¹⁰ Id.

1. Upon receipt of Form 12277 or an appropriate letter request, authorize withdrawal of an NFTL for taxpayers who meet the requisite criteria for:
 - a. already released NFLTs, and
 - b. Direct Debit Installment Payment Agreements.
2. Implement consistent training on when and how to authorize such “automatic” withdrawals of NFTLs.

ISSUE TWO: ELECTRONIC COMPLETION AND FILING SHOULD BE AVAILABLE FOR FORM 1099

Executive Summary

Small business owners are required to file Forms 1099 for payments made to non-incorporated businesses, vendors, and contractors. Form 1099-MISC is usually required. Currently, this form cannot be filed on-line from the IRS website. Businesses that do not have a large number of these forms to complete have limited options. The ability to complete and file the Form 1099-MISC on-line would reduce taxpayer burden by simplifying a business taxpayer's ability to comply with this tax requirement.

Background

When third party information is available to the IRS, tax compliance is significantly higher than when third party information is not provided. Additionally, the IRS has asked for IRSAC's input on opportunities for areas of improvement to reduce taxpayer burden without compromising compliance programs. Currently business owners who have a small number of Forms 1099-MISC to file have limited options:

1. They must pay their tax professional to prepare what is deemed a simple form;
2. order the forms from the IRS and wait for delivery;
3. purchase the forms at an office supply store and then complete the forms;
4. purchase a software program to complete the forms;
5. research and use one of the various commercial on-line 1099 preparation websites.

Although it may not seem an obvious issue, if the forms are purchased, the business owner still must find a way to complete them as prescribed by the IRS.

Completion of the forms is burdensome because most preparers prefer the forms to be typewritten even though, typewriters are no longer standard equipment in an office; and haphazardly, handwritten forms are considered unprofessional in a highly competitive business environment. There are on-line companies that offer this service for a small fee; however, in the current environment of tax fraud, scams from sites that look exactly like financial institutions, IRS phishing emails, and etc. business owners are hesitant to engage an unfamiliar company. Unfortunately, what should be one of the easier aspects of tax law to comply with becomes unnecessarily complicated and time consuming, discouraging businesses with less than twenty (20) Forms 1099-MISC from filing.

Currently business owners go on-line to research and complete a task immediately. This option is not available for Form 1099-MISC filters. Currently, the Tools menu path on www.irs.gov provides a Form 1099-MISC for informational purposes, but the form is not fillable. The IRS should facilitate the process of preparing small numbers of information returns for business owners. This will reduce taxpayer burdens and increase compliance as more taxpayers receive the appropriate Forms 1099-Misc for income earned.

Recommendations

1. Business owners go on-line to research and complete their task immediately. This option is not available for Form 1099-MISC. Currently through the Tools menu path on www.irs.gov the form for 1099-MISC is available to complete for informational purposes, but the form is not fileable. The IRS should allow taxpayers who have less than 20 Forms 1099-MISC to complete and file the

forms on www.irs.gov, similar to the Social Security Administration's process for Form W-2s.

2. Alternatively, similar to filing a Form 990-N postcard or the free-file program, the IRS should provide a link on the IRS website to approved Form 1099-MISC preparation providers with the appropriate warning that the taxpayer is leaving the IRS website.

ISSUE THREE: ENCOURAGE TAXPAYERS TO CORRECT UNDERREPORTING ON FORMS 1099 AND W-2

Executive Summary

Matching third party reporting of income is the most efficient audit technique available to the IRS. For that reason, it is important that information reporting be accurate. Too often, a taxpayer is not sure of what form to file. Given the volume of forms filed, some of these forms will have incorrect information. In a voluntary compliance tax system, taxpayers should be encouraged not only to report and pay the proper amount of tax on originally filed information returns, but also have the ability to discover and voluntarily correct errors as efficiently as possible. Administrative guidance, such as an announcement or revenue procedure, should be released that details how an information return preparer can efficiently correct returns, while opting to pay a compliance fee that satisfies any tax liability that the payee might have. With this, the Internal Revenue Manual should be revised accordingly.

Background

The third party information return filing system serves as a vital tool to both insure proper tax compliance and to combat fraud and identity theft. In 2010, the IRS reported that it closed 4.3 million cases in which a discrepancy was identified between the taxpayer return and third-party information, resulting in more than \$7.2 billion in additional assessments.¹¹ Further, Commissioner Shulman's "Real-time Tax System

¹¹ 2010 IRS Data Book

Initiative” envisions embedding “this core third-party information into our pre-screening filters, and would immediately reject any return that did not match up with our records.”

Undoubtedly, third party information return reporting has and will play an increasingly important role in tax administration and compliance enforcement. Currently, the IRS utilizes the Automated Underreporter (AUR) program to identify mismatches between tax returns and corresponding information returns. Three times a year, the AUR program matches the more than 140 million tax returns to a corresponding 1.8 billion information returns filed every tax year. The importance of this is highlighted by the new question on business information reporting forms. Taxpayers will now be required to sign under penalty of perjury that all filings have been made contained in tax forms (e.g., Form 1040 Schedules C, C-EZ, and F, and Forms 1120, 1120S and 1065) that require taxpayers to affirm their compliance with information reporting that must be completed on Forms 1099.

Even though there are inherent systemic ambiguities with determining which information returns are required to be completed and where and how to report different types of compensation on the forms, third parties nonetheless face the possibility of harsh penalties for getting it wrong. For example, for each timely filed return that does not include all required information or includes incorrect information, Section 6721 imposes a \$100 penalty per occurrence (up to \$1.5 million). Similar penalties apply under Section 6722 for failure to furnish taxpayers with complete and accurate information returns.

While Section 6721(c) provides penalty relief for inaccurate or incomplete information returns if such errors are de minimis,¹² more administrative correction programs are needed. If an error affects a handful of taxpayers in a significant way, it makes sense to issue a corrected Form W-2 or Form 1099, prompting the recipient to file an amended Form 1040 and pay the proper amount of tax. However, sometimes, an error affects hundreds or even thousands of taxpayers, each in an insignificant way, but with a significant aggregate effect. In those situations, it is inefficient to issue corrected Forms W-2 or Forms 1099 and require a large number of taxpayers to file amended Forms 1040 to make insignificant changes to their returns. Nevertheless, these errors should be corrected, not only because they are often significant in the aggregate, but because most taxpayers in our voluntary tax system want to be confident that the IRS forms filed are correct.

Given the finite resources available for IRS enforcement efforts and the voluntary nature of the U.S. tax system, entities responsible for the information reporting errors should be encouraged to discover and correct them. Upon discovering an underreporting error affecting a large population, each in a minor way, it should be possible for an entity to bring the error to the attention of the IRS and pay a negotiated sanction that approximates the actual tax liability the affected population would have paid if the error had not occurred. This approximation could be based on data from the Statistics of Income Bulletin, for example, or other information available to the taxpayer or the IRS.

¹² Limitations on de minimis relief include: (1) correcting the failure on or before August 1 in the required filing year, (2) for any calendar year the number of failed information returns shall not exceed 10 or one-half of 1 percent of the total number of information returns required to be filed by the person during the calendar year.

Under these circumstances unfortunately, the Internal Revenue Manual and taxpayers' anecdotal experiences are more discouraging than encouraging. For example, Internal Revenue Manual Exhibit 8.13.1-12 contains a pattern information reporting program closing agreement for understatement of income on Forms 1099 and states that "[i]n cases of underreported income brought to the attention of the Service by a payer, a rate of 28 percent will be applied to the total amount of the understated reportable income." In addition, Internal Revenue Manual Section 4.23.8.8 provides that the supplemental wage withholding rates (currently either 25 percent or 35 percent) generally should be used unless the employer can establish each employee's allowable number of exemptions from Form W-4. Because errors may be discovered years after they occurred, information regarding the Form W-4 is often not readily available and the supplemental rate would need to be used. These rates seem high, given that 94.2 percent of returns had marginal tax rates below 28 percent in 2009, (the last year for which data is available). *Kyle Mudry, Individual Tax Rates and Shares, 2009, in STATISTICS OF INCOME BULLETIN 20, at 25 (Winter 2012), available at <http://www.irs.gov/pub/irs-soi/12inwinbulratesshare.pdf>.* Likewise, employers have anecdotally found that the IRS has been increasingly unwilling to allow Form W-2 underreporting to be resolved by the employer without furnishing Forms W-2c or involving the affected employees, even when very small amounts of underreporting per employee are involved and the only change that needs to be reported once the issue has been resolved is a change in social security wages. Most employers want to provide the Social Security Administration with updated wage information if this could affect an employee's social security benefits, but

are reluctant to confuse their workforce with these forms when no amended returns need to be filed.

Recommendation

1. Issue administrative guidance and revise the Internal Revenue Manual to allow closing agreements to be entered into to correct underreporting errors on Forms 1099 and W-2 by having the entity responsible for the error pay a negotiated sanction approximating the actual tax liability the affected population would have paid if the error had not occurred. Also require Form W-2c to be prepared and filed with the Social Security Administration, only for those employees who have an increase in social security wages as a result of the additional reported income.
2. Publicize the ability of employers to use this closing agreement process to correct errors in both open and closed years, perhaps through issuance of a news release.

**ISSUE FOUR: PROVIDING FOR A CENTRAL AND ASSESSIBLE
INFORMATION SOURCE FOR TAXPAYERS, PARTICULARLY SMALL
BUSINESS TAXPAYERS, TO UNDERSTAND THEIR INFORMATION
REPORTING**

Executive Summary

Despite new statements contained in tax forms (e.g., Form 1040 Schedules C, C-EZ, E, and F, and Forms 1120, 1120S and 1065) that require taxpayers to affirm their compliance with Form 1099 information reporting, there is no entry point or checklist on the IRS website or in any of the publications that allows a taxpayer to easily determine its reporting requirements. While there is much information available, much of it is form specific and thus researching the specific form to file is difficult as it is really a process of trial and error.

Background

An increasing demand for third party information increases the taxpayer's reporting compliance burden. There are currently more than thirty (30) types of tax information returns required by the federal government.¹³ Those returns include Form W-2, which reports wages and other forms of compensation paid to employees. Completing Form W-2 often requires the third party to determine where and how on the form to report multiple types of compensation.¹⁴ In addition to the complexities of completing Form W-2, there are also other information reporting requirements imposed on third

¹³ IRS Publication - A Guide to Information Returns

¹⁴ Other forms of compensation that may trigger added Form W-2 reporting efforts, such as adding special codes, include: healthcare costs; dependent care; reimbursements; deferred compensation; sick pay; combat pay.

parties regarding non-wages. For example, those non-wage reporting requirements include, completing various Forms 1099 (16 types), Forms 1098 (four types), and Forms 5498 (three types). There are also forms that employees must complete and submit to an employer regarding withholding.

Recommendation

1. The IRS should publish flow charts and similar aids which can be used to determine what information return should be filed. Such aids should be available in IRS regulations or publications and on a central information reporting website.
2. The material below may provide a starting point for further development of consolidated information reporting library resource.

Forms 1098 and 1099 Reporting

Did I make or receive a payment to or from a business or another person during the calendar year?

I made a payment.

Was my payment a dividend or other distribution to a shareholder of the company?

Yes, go to **2**

Did I pay interest on a debt to someone? (excluding interest on an obligation issued by an individual)

Yes, go to **3**

Did I receive payment of mortgage interest (including points) in the course of my trade or business from individuals, or did I receive reimbursements of overpaid interest from them?

Yes, go to **9**

Did I have a reportable sale or exchange of real estate?

Yes, go to **4**

Did I make a distribution from a retirement or profit plan, or from an IRA or insurance contract?

Yes, go to **5**

Did I pay any of the following in the course of my trade or business (in some cases the amount must be \$600 or more, and other exceptions may apply as may other reporting requirements):
 (1) rent or royalties;
 (2) crewmembers of my fishing boat;
 (3) for services performed by independent contractors or others not employees of my business;
 (4) for physician's service or other health and medical services and a medical assistance program or health and accident program;
 (5) for a purchase of fish in excess of the reportable amount;
 (6) substitute dividends or tax-exempt interest payments and I am a broker;
 (7) crop insurance proceeds; or,
 (8) for services rendered to me by an attorney?

Yes, go to **6**

Did I release someone from paying a debt secured by property or otherwise forgive their debt to me? Or did they abandon property that was subject to the debt?

Yes, go to **1**

Am I a broker and did I sell a covered security belonging to my customer?

Yes, go to **8**

Am I an issuer of a security taking a specified corporate action that affects the cost basis of the securities held by others?

Yes, go to **8**

Am I a Payment Settlement Entity that makes payments to merchants and other entities in a payment card network?

Yes, go to **7**

Types of Payments

Below is an alphabetic list of some payments and the forms to file and report them. However, it is not a complete list of all payments, and the absence of a payment from the list does not indicate that the payment is not reportable. For instructions on a specific type of payment, see the separate instructions in the form(s) listed.

Type of Payment	Report on Form	Type of Payment	Report on Form
Abandonment	1099-A	Indian gaming profits paid to tribal members	1099-MISC
Accelerated death benefits	1099-LTC	Interest income	1099-INT
Acquisition of control	1099-CAP	Tax-exempt	1099-INT
Advance health insurance payments	1099-H	Interest, mortgage	1098
Agriculture payments	1099-G	IRA contributions	5498
Allocated tips	W-2	IRA distributions	1099-R
Alternate TAA payments	1099-G	Life insurance contract distributions	1099-LTC
Annuities	1099-R	Liquidation, distributions in	1099-DIV
Archer MSAs:		Loans, distribution from pension plan	1099-R
Contributions	5498-SA	Long-term care benefits	1099-LTC
Distributions	1099-SA	Medicare Advantage MSAs:	
Attorney, fees and gross proceeds	1099-MISC	Contributions	5498-SA
Auto reimbursements, employee	W-2	Distributions	1099-SA
Auto reimbursements, nonemployee	1099-MISC	Medical services	1099-MISC
Awards, employee	W-2	Merchant card payments	1099-K
Awards, nonemployee	1099-MISC	Mileage, employee	W-2
Barter exchange income	1099-B	Mileage, nonemployee	1099-MISC
Bond tax credit	1097-BTC	Military retirement	1099-R
Bonuses, employee	W-2	Mortgage insurance premiums	1098
Bonuses, nonemployee	1099-MISC	Mortgage interest	1098
Broker transactions	1099-B	Moving expense	W-2
Cancellation of debt	1099-C	Nonemployee compensation	1099-MISC
Capital gain distributions	1099-DIV	Nonqualified deferred compensation:	
Car expense, employee	W-2	Beneficiary	1099-R
Car expense, nonemployee	1099-MISC	Employee	W-2
Changes in capital structure	1099-CAP	Nonemployee	1099-MISC
Charitable gift annuities	1099-R	Original issue discount (OID)	1099-OID
Commissions, employee	W-2	Patronage dividends	1099-PATR
Commissions, nonemployee	1099-MISC	Pensions	1099-R
Commodities transactions	1099-B	Points	1098
Compensation, employee	W-2	Prizes, employee	W-2
Compensation, nonemployee	1099-MISC	Prizes, nonemployee	1099-MISC
Contributions of motor vehicles, boats, and airplanes	1098-C	Profit-sharing plan	1099-R
Cost of current life insurance protection	1099-R	Punitive damages	1099-MISC
Coverdell ESA contributions	5498-ESA	Qualified plan distributions	1099-R
Coverdell ESA distributions	1099-Q	Qualified tuition program payments	1099-Q
Crop insurance proceeds	1099-MISC	Real estate transactions	1099-S
Damages	1099-MISC	Recharacterized IRA contributions	1099-R, 5498
Death benefits	1099-R	Refund, state and local tax	1099-G
Accelerated	1099-LTC	Rents	1099-MISC
Debt cancellation	1099-C	Retirement	1099-R
Dependent care payments	W-2	Roth conversion IRA contributions	5498
Direct rollovers	1099-Q	Roth conversion IRA distributions	1099-R
Direct sales of consumer products for resale	1099-R, 5498	Roth IRA contributions	5498
Directors' fees	1099-MISC	Roth IRA distributions	1099-R
Discharge of indebtedness	1099-MISC	Royalties	1099-MISC
Dividends	1099-DIV	Timber, pay-as-cut contract	1099-S
Donation of motor vehicle	1098-C	Sales:	
Education loan interest	1098-E	Real estate	1099-S
Employee business expense reimbursement	W-2	Securities	1099-B
Employee compensation	W-2	Section 1035 exchange	1099-R
Excess deferrals, excess contributions, distributions of	1099-R	SEP contributions	W-2, 5498
Exercise of incentive stock option under section 422(b)	3921	SEP distributions	1099-R
Fees, employee	W-2	Severance pay	W-2
Fees, nonemployee	1099-MISC	Sick pay	W-2
Fishing boat crew members proceeds	1099-MISC	SIMPLE contributions	W-2, 5498
Fish purchases for cash	1099-MISC	SIMPLE distributions	1099-R
Foreclosures	1099-A	Student loan interest	1098-E
Foreign persons' income	1042-S	Substitute payments in lieu of dividends or tax-exempt interest	1099-MISC
401(k) contributions	W-2	Supplemental unemployment	W-2
404(k) dividend	1099-DIV	Tax refunds, state and local	1099-G
Gambling winnings	W-2G	Third-party network payments	1099-K
Golden parachute, employee	W-2	Tips	W-2
Golden parachute, nonemployee	1099-MISC	Transfer of stock acquired through an employee stock purchase plan under section 423(c)	3922
Grants, taxable	1099-G	Tuition	1098-T
Health care services	1099-MISC	Unemployment benefits	1099-G
Health insurance advance payments	1099-H	Vacation allowance, employee	W-2
Health savings accounts:		Vacation allowance, nonemployee	1099-MISC
Contributions	5498-SA	Wages	W-2
Distributions	1099-SA		
Income attributable to domestic production activities, deduction for	1099-PATR		
Income tax refunds, state and local	1099-G		

3. See the general instructions at <http://www.irs.gov/uac/General-Instructions-for-Certain-Information>Returns>.

	Form	Title	Subject Area	Dollar Threshold	Due Date to IRS	Due Date to Payee
①	1099-A	Acquisition of Abandonment of Secured Property	<p>File Form 1099-A, if in full or partial satisfaction of your trade or business debt, you acquire an interest in property that is security for the debt, or you have reason to know that the property has been abandoned. You need not be in the business of lending money to be subject to this reporting requirement.</p> <p>The requirements for this form are coordinated with the requirements for Form 1099-C.</p> <p>For more information on what must be reported and who must file, go to: http://www.irs.gov/instructions/i1099ac/ar01.html</p>	All reportable amounts.	February 28	January 31
	1099-C	Cancellation of Debt	<p>Cancellation or discharge of a debt owed to a financial institution, the Federal Govt., credit union, etc. or any organization in a significant trade or business of which is lending money</p> <p>For more information on what must be reported and who must file, go to: http://www.irs.gov/instructions/i1099ac/ar01.html</p>	\$600 or more	February 28	January 31
②	1099-DIV	Dividends and Distributions	<p>Distribution, such as dividends, capital gain distributions, or nontaxable distribution, that were paid on stock and liquidation distributions</p> <p>For more information on what must be reported and who must file, go to: http://www.irs.gov/instructions/i1099div/index.html</p>	\$10 or more, except \$600 or more for liquidations	February 28	January 31

③	1099-INT	Interest Income	<p>Interest income</p> <p>For more information on what must be reported and who must file, go to: http://www.irs.gov/instructions/i1099int/index.html</p>	\$10 or more (\$600 or more in some cases)	February 28	January 31
④	1099-S	Proceeds from Real Estate transaction	<p>Gross proceeds from the sales or exchange of real estate from reportable transactions.</p> <p>For more information on what must be reported and who must file, go to: http://www.irs.gov/instructions/i1099s/index.html</p>		February 28	January 31
⑤	1099-R	Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.	<p>Distributions from pensions and annuities, retirement or profit-sharing plans, any IRA, or insurance contracts, and IRA recharacterizations</p> <p>For more information on what must be reported and who must file, go to: http://www.irs.gov/instructions/i1099r/index.html</p>	\$10 or more	February 28	January 31
⑥	1099-MISC	Miscellaneous Income	<p>For more information on what must be reported and who must file, go to: http://www.irs.gov/instructions/i1099misc/ar01.html</p>		Generally February 28	Generally January 31
			Rent or royalty payments; prizes and awards that are not for services (such as winnings on TV or radio shows)	\$600 or more, except \$10 or more royalties		
			Payments to crewmembers by owners or operators of fishing boats including payments of proceeds from sale of catch	All amounts		
			Payments for services performed for a trade or business by people not treated as its employees. (For example, fees to subcontractors or directors, accountants, or for items like business equipment repairs)	\$600 or more		

			<p>Payments to physicians, physicians' corporation, or other supplier of health and medical services. Issued mainly by medical assistance programs or health and accident insurance plans</p>	\$600 or more		
			Fish purchases for cash	\$600 or more		
			Crop insurance proceeds	\$600 or more		
			<p>Substitute dividend and tax-exempt interest payments reportable by brokers</p> <p>(Due date to payee is February 15)</p>	\$10 or more		
			<p>Gross proceeds paid to attorneys</p> <p>(Due date to payee is February 15)</p>	All amounts		
7	1099-K	Merchant Card and Third Party Network Payments	<p>Beginning in January, 2012, payment settlement entities (PSEs) are required by the Housing Assistance Tax Act of 2008 to report on Form 1099-K the following transactions:</p> <p>All payments made in settlement of payment card transactions (e.g., credit card);</p> <p>Payments in settlement of third party network transactions IF:</p> <ul style="list-style-type: none"> -Gross payments to a participating payee exceed \$20,000; AND -There are more than 200 transactions with the participating payee. <p>For more information on what must be reported and who must file, go to: http://www.irs.gov/businesses/article/0,,id=251489,00.html</p> <p>See also: http://www.irs.gov/taxpros/article/0,,id=225080,00.html</p>			
8	1099-B	Proceeds From Broker and Barter	<p>Sales or redemptions of securities, futures transactions, commodities, and barter exchange transactions.</p> <p>Section 403 of the Energy Improvement and Extension Act</p>			February 15

		Exchange Transactions	<p>of 2008 amended the Internal Revenue Code to mandate that every broker required to file a return with the IRS reporting gross proceeds from the sale of a covered security additionally report a customer's adjusted basis in the security and whether any gain or loss on the sale is classified as short-term or long-term. Additionally, the amendments direct brokers to follow customers' instructions and elections when determining adjusted basis. The amendments also provide that, when a broker transfers securities to another new broker before their sale, the transferring broker must furnish to the receiving broker a statement containing sufficient information about the transferred securities for the receiving broker to determine the customer's adjusted basis and whether any gain or loss is short-term or long-term when the transferred security is eventually sold. Finally, the amendments require issuers of securities to file a return with the IRS and furnish a statement to holders of the securities after taking a corporate action that affects the basis of the security to explain the corporate action and its quantitative effect upon the basis of the security.</p> <p>For more information on what must be reported and who must file, go to: http://www.irs.gov/taxpros/article/0,,id=237099,00.html</p> <p>See also: http://www.irs.gov/taxpros/article/0,,id=225080,00.html</p>			
9	1098	Mortgage Interest Statement	<p>Mortgage interest (including points) you received in the course of your trade or business from individuals and reimbursements of overpaid interest</p> <p>For more information on what must be reported and who must file, go to: http://www.irs.gov/instructions/i1098/index.html</p>	\$600 or more	February 28	To Payer or Borrower by January 31
	W-2	Wage & Tax Statement	<p>Wages, tips, other compensation, social security, Medicare, withheld income taxes.</p> <p>See Publication 15 for additional info.</p>	See form instructions.	Only to SSA.	January 31
	W-2G	Certain Gambling Winnings	<p>Gambling winnings from horse racing, dog racing jai alai, lotteries, keno, bingo, slot machines, etc.</p>	Generally, \$600 or more. \$1200 or more from	February 28	January 31

				bingo or slot machines. \$1500 or more from keno.		
	W-3	Transmittal of Wage & Tax Statements	Used to transmit Copy A of Forms W-2, Wage & Tax Statement.	Summary of W-2 amounts.	February 28	N/A
	945	Annual Return of Withhold Federal Income Tax	Federal tax withheld on Forms 1099 and W-2G must be reported on Form 945.	All amounts withheld from nonpayroll payments.	January 31 following the tax year (or by Feb. 10, if deposits were timely paid in full for the year).	N/A
	1042	Annual Withholding Tax Return for US Source Income of Foreign Persons	<p>Tax withheld of certain income of nonresident aliens, foreign partnerships, foreign corporations, and nonresident alien or foreign fiduciaries of estates or trusts, and to transmit paper Forms 1042-S</p> <p>For more information on what must be reported and who must file, go to: http://www.irs.gov/formspubs/article/0,,id=242311,00.html </p>	All amounts	March 15	N/A
	1042-S	Foreign Person's US Source Income Subject to Withholding	Payments subject to withholding under Chapter 3 of the Code, including interest, dividends, royalties, pensions and annuities, gambling winnings, and compensation for personal services	All amounts	March 15	March 15
	1042-T	Annual Summary and Transmittal of Forms 1042-S				

	1096	Annual Summary and Transmittal of US Information Return	Used to transmit paper Forms 1099, 1098, 5498, and W-2G For more information on what must be reported and who must file, go to: http://www.irs.gov/formspubs/article/0,,id=239516,00.html	Uses information taken from Forms 1099, 1098, 5498 & W2-G	February 28	N/A
	FinCEN Form 104	Currency Transaction Report	Each deposit, withdrawal, exchange of currency, or other payment or transfer by, through, or to financial institutions (other than casinos).	Over \$10,000.	15 days after date of transaction.	Not required.
	5754	Statement by Person Receiving Gambling Winnings	Amount of gambling winnings you received for someone else or as a member of a group of winners on the same winning ticket.	Name, taxpayer ID, address, amount won, & winnings from identical wagers for each winner.	N/A.	To be given to payer of winnings.
	8027	Employer's Annual Information Return of Tip Income & Allocated Tips	Large food and beverage establishments when the employer is required to make annual reports to the IRS on receipts from food or beverage operations and tips reported by employees.	If applicable, form must be completed using the employer's records of tips.	February 28	N/A
	8300	Report of Cash Payments Over \$10,000 Received in a Trade or Business	Payment in cash or foreign currency received in one transaction, or two or more related transactions, in the course of a trade or business. Does not apply to those required to file Form 4789; casinos required to file Form 8362; or, generally, transactions outside of the U.S.	Over \$10,000	15 days after date of transaction	To Payer by January 31

	FinCEN Form 103	Currency Transaction Report by Casino (CRTC)	Each transaction involving either currency received (cash-in) or currency disbursed (cash-out) of more than \$10,000 in a gaming day.	Over \$10,000.	15 days after date of transaction.	N/A
--	-----------------------	----------------------------------------------------------	---------------------------------------------------------------------------------------------------------------------------------------	-------------------	---------------------------------------------	-----

In addition to information required on returns that compute a liability for a tax, other information reporting may be required instead of or in addition to those provided above:

- Form 1065, U.S. Return of Partnership Income (including Schedules K-1);
- Form 1120S, U.S. Income Tax Return for an S Corporation (including Schedules K-1);
- Form 5500, Annual Return/Report of Employee Benefit Plan;
- Form 8038, Information Return for Tax-Exempt Private Activity Bond Issues;
- Form 8038-G, Information Return for Government Purpose Tax-Exempt Bond Issues;
- Form 8038-GC, Consolidated Information Return for Small Tax-Exempt Government Bond Issues;
- Form W-8BEN, Beneficial Owner's Certificate of Foreign Status for U.S. Tax Withholding;
- Form SS-8, Determination of Worker Status;
- Form 990, Return of Organization Exempt from Income Tax;
- Form 990-EZ, Short Form Return of Organization Exempt From Income Tax;
- Form 990-N, Electronic Notice (e-Postcard) for Tax-Exempt Organizations not Required To File Form 990 or 990-EZ;

- Form 1040-ES, Estimated Tax for Individuals;
- Form 1120-W, Estimated Tax for Corporations;
- Form 2350, Application for Extension of Time to File U.S. Income Tax Return;
- Form 2350 (SP), Application for Extension of Time to File U.S. Income tax Return (Spanish Version);
- Form 4137, Social Security and Medicare Tax on Unreported Tip Income;
- Form 4768, Application for Extension of Time to File a Return and/or Pay U.S. Estate (and Generation-Skipping Transfer) Taxes;
- Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return;
- Form 4868 (SP), Application for Automatic Extension of Time to File U.S. Individual Income Tax Return (Spanish Version);
- Form 5558, Application for Extension of Time to File Certain Employee Plan Returns;
- Form 7004, Application for Automatic 6-Month Extension of Time To File Certain Business Income Tax, Information, and Other Returns;
- Form 8109, Federal Tax Deposit Coupon;
- Form 8027, Employer's Annual Information Return of Tip Income and Allocated Tips;
- Form 8809, Application for Extension of Time to File Information Returns;
- Form 8868, Application for Extension of Time To File an Exempt Organization Return;

- Form 8892, Application for Automatic Extension of Time to File Form 709 and/or Payment of Gift/Generation-Skipping Transfer Tax;
- Form 8919, Uncollected Social Security and Medicare Tax on Wages;
- Form 3520, Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts;
- Form 3520-A, Annual Information Return of Foreign Trust With a U.S. Owner (Under section 6048(b));
- Form 5471, Information Return of U.S. Persons With Respect To Certain Foreign Corporations;
- Form 5472, Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business (Under Sections 6038A and 6038C of the Internal Revenue Code);
- Form 8805, Foreign Partner's Information Statement of Section 1446 Withholding Tax;
- Form 8858, Information Return of U.S. Persons With Respect To Foreign Disregarded Entities;
- Form 8865, Return of U.S. Persons With Respect to Certain Foreign Partnerships;
- Form 8288-A, Statement of Withholding on Dispositions by Foreign Persons of U.S. Real Property Interests;
- Form 8288-B, Application for Withholding Certificate for Dispositions by Foreign Persons of U.S. Real Property Interests;
- Form 8938, Statement of Specified Foreign Financial Assets;
- Form 926, Return by a U.S. Transferor of Property to a Foreign Corporation;

- Form 8621, Return by a Shareholder of a Passive Foreign Investment Company or Qualified Electing Fund;
- Form 8865, Return of U.S. Persons With Respect to Certain Foreign Partnerships;
- Form 8858, Information Return of U.S. Persons With Respect To Foreign Disregarded Entities;
- Form 5713, International Boycott Report.

Other information reports outside the Internal Revenue Code and associated regulations that are also required include the Form 90-22.1, Report of Foreign Bank and Financial Accounts.

For these and other forms, see <http://www.irs.gov/instructions/index.html>.

II. IRS Non-Filer Compliance Sustainance, and Enforcement

ISSUE FIVE: EFFICIENCIES IN IRS OUTREACH CAN BE CREATED TO BRING MORE TAXPAYERS INTO FILING AND PAYMENT COMPLIANCE.

Executive Summary

The IRS should consider expanding its educational outreach program to non-filer and delinquent taxpayers by focusing on small businesses and ethnic communities through a combination of public and social media, print and internet announcements, and personal contacts that will encourage filing of delinquent returns and payment of tax through a better awareness and understanding of available installment plans, offers in compromise, penalty abatement programs, and by tax preparation assistance.

Background

Individual and small business non-filers and delinquent taxpayers who potentially contribute to the tax gap range from those who have simply stopped filing for unknown reasons, to those who know they owe taxes but might be afraid of the consequences of filing or contacting the IRS, to those who attempt to evade the payment of tax altogether. Non-filers and taxpayers who are delinquent, but who otherwise want to get back into the system, would benefit from outreach programs since they offer a way to help the taxpayers comply sooner, allowing them to reduce accruing penalties and interest and take advantage of outstanding refunds, while bringing in tax dollars and making future compliance more likely. Successful approaches to these different groups may vary.

Identifying the non-filers. The first problem is how to identify the non-filers. The IRS has existing data and programs that can assist in identifying such persons and businesses, such as:

1. Matching programs through 1099s and W-2s, IMF¹⁵ and BMF¹⁶
2. Whistleblower program
3. Report of Foreign Bank and Financial Accounts (FBAR)
4. Currency transaction reports
5. Estate tax returns
6. K-1 reporting

Other sources the IRS should consider that may deem effective in identifying non-filers are:

1. State sales tax and unemployment tax filings
2. Credit card information
3. Professional license renewals
4. Loan applications
5. Lists of membership in chambers of commerce or trade groups

Communication with Targeted Communities. Appropriate and effective communication to taxpayers often depends on the community being targeted, whether it is an individual or a small business within an ethnic group, those in lower or upper income groups in general, or professional/trade groups. For instance, communication to the ethnic communities varies depending on the culture. Many of these groups use tax preparation services with employees who can communicate in their language. Outreach to such qualified tax preparers with their involvement in community education would assist in the goal of educating the non-filing taxpayer into filing and payment compliance.

¹⁵ Individual Master File

¹⁶ Business Master File

Much information can be spread by word of mouth in these communities. In addition, low budget advertising on trains, buses or billboards in the community is a cost effective way to bring the outreach program into the public eye on a daily basis.

Various other targeted groups of taxpayers can be targeted based on outreach to trade and professional groups, by advertising at schools, health clinics, churches, public transportation, and by radio and internet. Private tax assistance companies have been effective in getting their ads to the taxpayers desperate for assistance with their compliance needs in these ways. The IRS could reach its targeted markets in the same manner.

Voluntary Compliance. Voluntary compliance programs have been suggested as a possible answer to bringing non-filers and otherwise delinquent taxpayers back into filing and payment compliance by offering a way to pay past due taxes, while reducing penalties and possibly interest. For a successful example, in 2010, the state of Illinois publicized a tax program that allowed taxpayers to reduce the penalties and interest due on their past due tax balances if such balances were paid in full. To add a level of urgency to the program, the acceptance period was available for only a short period of time (5 weeks). If delinquent taxpayers chose to not avail themselves of the program, their penalties and interest then doubled after the expiration of the program period. Many taxpayers took advantage of the program and the state of Illinois realized approximately 25 percent more revenue than it had originally anticipated.¹⁷ The IRS offshore FBAR program had great success with graduated penalty programs publicity that brought many

¹⁷ Chicago Tribune, "More deadbeats pay up during Illinois' tax amnesty than expected." December 6, 2010.

delinquent taxpayers into the system and into compliance. The IRS first time and reasonable cause penalty abatements should also be publicized to attract taxpayers to contact the IRS to discuss their compliance issues.

Personal Outreach. According to the Taxpayer Advocate's 2011 Annual Report to Congress, one of the most serious identified problems was that the IRS does not emphasize the importance of personal taxpayer contact as an effective tax collection tool. Its studies showed that personal contact from the IRS was more effective than alternative collection activities in bringing in tax dollars. A phone call from the IRS is hard to ignore and taxpayers generally respond quickly, either by returning the call themselves, or by contacting a tax professional to assist them. The Taxpayer Advocate suggests that a simple phone call early on in the collection process can be more cost effective than other approaches such as the Substitute for Return (SFR) system for non-filers discussed below.¹⁸

Enforcement of Non-Filers. Once non-filer taxpayers have been identified, "soft notices" such as the CP 59¹⁹ or CP259²⁰ are sent notifying the taxpayer that a return(s) has not been filed. As to the individual taxpayer, the notice informs the non-filer that he will need to contact the IRS if he doesn't believe a tax return is due, or to seek assistance with filing and payment of tax if one is due. Once the soft notice letter is sent with no response received, a second letter or notice similar to (Letter 4903) is sent prior to an SFR being prepared and a tax assessed. These soft notices are not particularly

¹⁸ National Taxpayer Advocate's Report to Congress, December, 2011, page 344.

¹⁹ For individual taxpayers

²⁰ For business taxpayers

threatening, but they do not address the concern that the taxpayer will often have – how to file a tax return that is most likely several years old. Therefore, it would be beneficial to list a primary source of assistance under “What to do immediately” rather than under “Additional information” on the second page.

If the IRS does not hear from the taxpayers, and it already has information available, through Forms W-2, 1099, etc., it may create an SFR as the next step²¹, it may attempt to contact the taxpayer by telephone, or it may assign the case to the field. The SFR should be the last alternative only after making attempts to contact the taxpayer by phone or in person since those approaches may be more effective (IRS and TAS studies are on-going).

When the SFR is sent to the taxpayer, it may prompt the taxpayer to create his/her own return since an SFR does not allow for deductions, exemptions, credits, etc., and simply shows the income that the IRS has confirmed from third party input. Sometimes overinflated numbers provided by creating an SFR will be the impetus for the taxpayer to come to talk to the IRS. If the SFR has been prepared and the taxpayer is still not in contact with the IRS, the IRS has other programs that can be used to assist in developing and maintaining taxpayer compliance to pay the tax assessed by the SFR, including the Withholding Compliance and the Refund Hold programs. In combination, the SFR, Withholding Compliance and Refund Hold programs not only provide a way to pay the assessment, but further encourage the taxpayer to contact the IRS or to file a return in hopes of obtaining a refund based on actual deductions and credits that are not available through the SFR program.

²¹ IRM 4.12.1.1.3 (10-5-2010); IRM 4.12.1.8.2.2 (10-5-2010)

Recommendations

1. Solicit the taxpayer's voluntary cooperation with filing or securing a delinquency by providing additional information in the soft notices. The soft notices should be solution-based.
2. Direct the taxpayer, through both soft notices and outreach, to contact a local income tax clinic, local bar association or accounting group for filing assistance since many delinquent taxpayers require such assistance. Taxpayers should be cautioned to seek out a reputable tax preparer, such as one listed as a qualified preparer on www.irs.gov, and not turn to questionable tax preparation companies for assistance.
3. Direct the taxpayer to contact the IRS help line for further direction by placing the phone number in "how to file" and "how to pay" sections of all soft notice letters.
4. Consider sending a soft notice when an SFR is generated, explaining how to potentially reduce the assessment.
5. Provide outreach for the non-filing compliance program and payment arrangement programs for delinquent accounts. Low budget advertising such as billboards in ethnic communities, prominent spots on the IRS web page, internet banners or margin ads on major community newspaper sites, print flyers in community advertisement mailing, and recorded messages played on the IRS customer service lines while the taxpayer is on hold are low cost ways to get the program in front of the targeted groups.

6. Combine internal IRS programs so that information can be better accessed, more easily shared; provide a one source approach to the taxpayer and tax professional communities and cut costs.
7. First time and reasonable cause penalty abatement programs and non-filer tax days at IRS centers should be publicized to bring taxpayers in to discuss their tax accounts with a representative.

III: Opportunities for Technology Improvements

ISSUE SIX: USE OF ACCOUNTING SOFTWARE DURING EXAMINATIONS REDUCES BURDENS TO TAXPAYERS AND THE SERVICE, BUT SHOULD BE CAREFULLY LIMITED IN ITS IMPLEMENTATION

Executive Summary

Taxpayers and their advisers are inherently cautious when confronted with an IRS request for records and other data in the context of an examination of the taxpayer's return for a particular period. This may be because of concerns about defining the scope of the audit or for other reasons. Similarly, the IRS has concerns about obtaining all relevant information and its integrity.

Use of electronic data is an efficient examination tool for the IRS as it reduces the amount of paper generated for examinations and in some cases the time required to complete them. But IRS requests for electronic client backup files from commercially available business software programs (e.g., QuickBooks, and Peachtree) now used by many small businesses have heightened concerns by affected taxpayers and their advisers about the breadth of information requested by the IRS and the use of that information.

The chief concerns among these are:

- The wide range of data included in the electronic file, including nonaccounting information such as customer data;
- The number of years of data, outside those under examination, that are potentially available to the examiner; and,
- Use of metadata in the files that may indicate access and modification of the data in the file – particularly where those modifications are performed outside the

accounting period in question (e.g., those modifications may indicate improper activity, but are much more likely to indicate simple error corrections or adjustments made necessary by circumstances in a later period that are somehow related to the transaction in question).

- Meeting the record retention requirements of Rev. Rul. 71-20, 1971-1 C.B. 392 and Rev. Proc. 98-25, 1998-1 C.B. 689 with respect to electronic books and records, particularly in a small business context.

These concerns limit taxpayer willingness to adopt the new approaches and should be accompanied by reasonable safeguards.

Background

The IRS announced in October, 2010 that it was expanding its audit capabilities by training agents to be proficient in auditing information from files of accounting software commonly used by small businesses. In addition to training examiners on use of the software, the IRS moved forward with increased requests of electronic files from taxpayers and practitioners. Practitioners had indicated that they wanted the IRS to be more efficient in examining records and to reduce the volume of paper involved in audits.

On May 27 and on August 9, 2011, the IRS modified IRM 4.10.4.3.7.5 to provide guidance and rules on how revenue agents should evaluate taxpayers' electronic books and records. The IRS description of electronic books and records also includes taxpayer websites, e-commerce activities and web marketing material, which the IRS finds useful in evaluating audit trails and for tracing income, such as e-payments.

On September 1, 2011, SB/SE issued a field directive (SBSE-04-0911-086) for examiners with respect to requests to review backup files and how to protect them. It also updated a set of frequently asked questions (FAQs).

The directive generally instructs examiners to request a copy of the taxpayer's original software backup file but to use professional judgment when determining which records to request. For example, agents would likely request electronic files in larger-scope audits (e.g., to verify items like gross income), but would not likely request files in an audit of one expense item. The memo and FAQs state that agents will limit their review to information relevant to the year under examination. However, if the IRS is examining certain issues, such as accrual accounting or reconstruction of income, then it might review relevant data from other tax periods. Based on the results of an examination, the IRS also might expand the scope of an audit. In that case, the IRS would notify the taxpayer and use the available records.

The directive states that agents would not use the files for any purposes other than the examination and that the information is not subject to disclosure to the public. When taxpayers or practitioners assert they cannot comply because the backup file contains "privileged information," such as information protected under the Health Insurance Portability and Accountability Act of 1996, the taxpayer representative should speak to the IRS agent about redaction. The directive suggests examiners contact their local IRS counsel for assistance.

Redactions to requested files can be an issue. IRS examiners review and assess original books of entry—not translated or interpreted or redacted versions. In addition to the financial information provided in the electronic file, the original file may also contain

metadata including audit trails that can be used to assess the reliability of the records.

Audit trails allow the examiner to view original transactions, subsequent changes, and the user name of the person who entered or changed a transaction. This information may be directly relevant to the evaluation of the taxpayer's accounting system and internal controls.

The IRS has commented publicly about taxpayers' providing redacted prior-year files. On April 20, 2011, then SB/SE Commissioner Wagner addressed the redaction issue in a letter to the AICPA. The letter confirmed the long-standing position of the IRS to have original documentation in an audit.

It is important an exact copy of the original electronic data file be provided to the examiner and not an altered version. Only an exact copy of the original file includes the unaltered metadata which allows examiners to properly consider the integrity and veracity of the electronic files through use of such means as reports generated by the software program that may help to identify deleted or altered entries.

The letter stated that it's acceptable for practitioners to "condense" prior-year information "as long as the condensed data does not include transactions created or changed for time periods under audit, or for transactions from prior years that have an effect on the years under audit." The IRS published its approval of this position in its FAQs, where the IRS also pointed out that, if the audit scope is expanded, the agent might request a backup file created before the file was condensed or a copy of the archive file created during the condensing process.

The letter also noted a software limitation best solved by software companies—allowing users to create backup files for a specified time period. However, many small

business persons are unaware of the availability of the redaction features found in the current commercial accounting software. This unawareness leads the small business taxpayer to be burdened with the notion they must provide more information to the IRS than is needed for the examination; all while being burdened with client privacy issues.

Recommendations

Reasonable safeguards should be available to protect small business taxpayers from turning over more data in an electronic format than is necessary for the IRS to perform an examination. A taxpayer should have the right to “redact” the software file and turn over only the data that is responsive and relevant to the examination. IRS should continue to work with taxpayers and taxpayer groups to refine these procedures and provide more definitive guidance responsive to these concerns.

1. On-going outreach to the AICPA, ABA Tax Section, and other practitioner groups and software manufacturers to identify means on limiting information to data requested by the IRS should be made possible.

ISSUE SEVEN: HMTL PAGES ON IRS.GOV SHOULD BE CONVERTED INTO PDF FORMAT FOR RETENTION, STORAGE, AND TRANSFERS TO CLIENTS

Executive Summary

The IRS Office of Online Services and other IRS offices have made enormous progress in making www.irs.gov a very important source of taxpayer guidance on many topics of concern to taxpayers and their advisers. The information is generally only available in Html format. That makes it difficult to share the information with others and to archive the information in a file or as a file. As the website becomes the primary source and in some cases the only repository of information, the inability to easily retain and transfer information become problematic.

Background

The pages on www.irs.gov contain general information about many IRS programs and offices, filing issues of concern to taxpayers, information about tax law enforcement programs, guidance on specific technical tax law issues and other critical guidance. Guidance may take the form of Frequently Asked Questions (FAQs) or other statements on particular pages related to an issue or return. These statements may be updated and changed from time to time or entirely deleted without warning.

Taxpayers and their advisers need a mechanism to share the information with others, and in many cases to archive the statements with an expectation to refer to them if particular actions resulting from reliance upon them are questioned at a later time.

The format of the pages on the IRS public internet website is the customary html page as ubiquitously used in almost all public websites. Most of the information is therefore available only in that format. It is difficult to archive the information. To store

the information in an electronic format often requires saving the page in a file as a web page rather than in some other storage format such as a Portable Document Format file (PDF) or a word processing program file. Further, printing the html pages may not work well in some circumstances (e.g., some headers or other page elements may not print or may be distorted or out of position in the printed copy of the page).

Because a file saved as a web page file in the Windows operating system contains html programming code, the email transmission of such a file may be quarantined by many corporate and Internet Service Provider spam filters as a possible threat to the security of the system.

The IRS should consider other sources that have adopted the mechanism that have the capabilities for converting document formats. As an example of a website system that has adopted such an approach, one might consider the (PDF) links on most informational pages of the Tax Analysts web service available to its subscribers. Another approach was adopted by Bloomberg BNA in its tax services available to subscribers that allows the page to be printed in a “printer friendly version for full-screen viewing and printing from the browser” (including printing in some .pdf file creation software programs) or in a “rich text format for importing into a word processing program” (e.g., Microsoft Word). Some blended approach of these two is preferable: all pages should be capable of being saved as a .pdf file in at least the format in which the words appear on the page, but for documents such as revenue procedures, revenue rulings, regulations, division field directives and other memoranda, most users would prefer to be able to download and save the document in a .pdf that captures the document in its original formatting (i.e., on

IRS letterhead, etc. as it was released to internal offices and to external organizations like the Federal Register or press agencies).

Recommendations

1. Provide a facility on each page of www.irs.gov, or at least those pages that contain information that taxpayers or advisers are likely to want to archive, to download or convert the page to .pdf format.